ANALYSIS OF ORIGINAL BILL

Author:	Cogdill	Analyst:	Jane Tolman	Bill Number:	AB 81XX
Related Bills:	See Legislative History	Telephone:	844-6111	Introduced Date:	July 10, 2001
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Energy Conservation Measures Deduction

SUMMARY

This bill would allow a deduction for energy conservation measures for residential dwellings or small commercial buildings in this state.

PURPOSE OF THE BILL

According to the author's staff, the purpose of this bill is to promote permanent energy load reduction and improve energy efficiency.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately and operative for taxable years beginning on or after January 1, 2001.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Current federal law provides two energy-related credits: an energy investment credit, and a business credit for the production of electricity from certain renewable resources.

Current state law does not provide for any energy-related credits or deductions.

Current state and federal laws generally allow taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business. However, expenses for acquiring property with a useful life in excess of a year or purchases that add to the value or substantially extend the useful life of property owned by the taxpayer must be capitalized and depreciated over the recovery period of the property rather than deducted in the year acquired.

Board Position:			Department Director	Date
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THIS BILL

Under the Personal Income Tax Law (PITL) and the Bank and Corporation Tax Law (B&CTL), this bill would allow a deduction equal to 25% of the cost of installing energy conservation measures. The deduction would be limited to $750 for a residential dwelling and $1,500 for a small commercial building for each year. The bill would define several terms, including “energy load reduction systems,” “passive systems,” and “small commercial building.”

The deduction allowed by this bill would be in addition to any other allowed deductions or credits.

IMPLEMENTATION CONSIDERATIONS

This bill would create a credit that requires an energy conservation measure to be installed by a “professional installer licensed by the state.” “Professional installer“ is undefined and it is unclear who within the state would license the professional installer.

It is unclear if “cost” would be limited to the principal price of the energy conservation measure or would it include interest and other possible financing costs.

The deduction would be limited to $750 for a residential dwelling and $1,500 for a small commercial building for each year. However, it is unclear whether that limitation would be applied for each taxpayer or for each building owned by the taxpayer.

After resolution of these concerns, implementation of this bill should not significantly impact the department’s programs and operations.

LEGISLATIVE HISTORY

ABX 27 and **AB 1124** (Koretz, 2001/2002) would allow multiple credits and an accelerated depreciation deduction for the purchase of a power generation system. **ABX 27** failed passage from the Assembly Appropriations Committee, and **AB 1124** failed passage from the Assembly Utilities and Commerce Committee. **SB 17** (Brulte, 2001/2002) would allow a credit for the purchase and installation of a solar energy system for the production of electricity. This bill is from Assembly without further action. **SBXX 17** is in the Assembly Revenue and Taxation Committee. **AB 873** (Takasugi, 1997/1998) would have allowed a credit equal to 40% of the cost of energy conservation measures. The bill also would have allowed a second credit equal to 10% of the cost of a solar energy system installed on premises located in California and used for commercial purposes, subject to certain requirements. The bill failed to pass the Assembly Revenue and Taxation Committee. **AB 654** (Horton, 2001/2002) and **ABXX 25** (Horton, 2001/2002) both would allow a refundable credit for individuals and a deduction for all taxpayers that purchase and install energy efficient residential appliances or energy conservation measures. Both bills remain in Assembly Revenue and Taxation Committee.

OTHER STATES' INFORMATION

Florida exempts from sales and use taxes certain energy-related activities, such as the manufacture of or the machinery or equipment used to produce electrical or steam energy. Solar energy systems and components of solar energy systems are tax-exempt through June 30, 2002.

Massachusetts currently has an energy credit that is equal to 15% of the net expenditures or $1,000, whichever is less. However, Massachusetts does not allow an energy-related deduction, but exempts a limited portion of local property tax for certain alternative energy systems, such as solar or wind powered systems or hydropower facilities built after 1978.

Michigan does not allow an energy-related credit or deduction, but exempts the value of energy conservation devices from the local property tax.

New York allows, for personal income taxpayers only, a credit for solar generating equipment equal to 25% of certain solar generating expenditures. The credit is capped at $3,700 per system. New York also exempts from property tax for 15 years any increase in assessed value of real property due to the value of a solar or wind energy system approved by the New York State Energy Research and Development Authority.

Oregon has two energy credits: a PIT consumer energy purchases credit and a corporate tax credit for the cost of energy projects. The consumer energy purchases credit allows various credits ranging from $50 to $1,500 for consumer purchases of certain items. The corporate credit for the cost of energy projects is a credit equal to 35% of the incremental cost of the project involving energy conservation and other related projects.

Texas does not allow an energy-related credit or deduction, but exempts from sales or use tax the repair, remodeling, maintenance, or restoration services on intangible personal property used to conserve energy.

FISCAL IMPACT

Once the implementation concerns are resolved, this bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

Based on data and assumptions discussed below, this bill would result in revenue losses on the order of $4 million annually beginning in 2001-02.

Revenue Discussion

The revenue impact of this bill would be determined by the amount of costs incurred by taxpayers for qualified energy conservation measures with respect to any residential dwelling or small commercial building in the state and by marginal tax rates of taxpayers incurring such costs.

In California, there are roughly 12 million residential structures/units and 485,000 nongovernmental owned commercial buildings. The number of commercial buildings that would qualify under the bill as “small” is unknown. For purposes of deriving a revenue estimate, it is assumed that half would qualify. Qualified energy conservation measures and costs (any passive system capable of saving a minimum of 5% in the amount of energy for cooling) that may be claimed as deductions by taxpayers can range in cost from a few hundred dollars for additional insulation to several thousand dollars for a replacement roof. In any given year, if 5% of households and 5% of small commercial building owners incur average costs of $2,500 and $5,000 respectively, qualified costs would total $1.5 billion for households and $60 million for small commercial building owners, of which 25% is potentially deductible under the proposal.

The potential state revenue loss would be $2.4 million for households and $1.2 million for small commercial building owners assuming an 8% tax rate. For households, the revenue loss assumes that only 8% of potentially deductible qualified costs would reduce income. As a miscellaneous itemized deduction, costs for qualified energy conservation measures would be included with other miscellaneous itemized deductions, if any, and would be deductible only to the extent they exceed 2% of adjusted gross income

ARGUMENTS/POLICY CONCERNS

This bill allows both this deduction and any existing deduction authorized under current law for the same item of expense. A business could expense the smaller items or depreciate the more expensive items, thus claiming a 125% deduction; however, if the basis is reduced, a federal/state difference will be created

This bill would require a professional licensed installer to install the energy system in order for the credit to be claimed. Thus, a homeowner who installs the system would not be eligible for the credit, even though the author’s intent of conserving energy would be achieved.

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